

Internal Revenue Service

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Person To Contact: _____, ID No. _____

Telephone Number: _____

Refer Reply To:
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Date:
September 13, 2007

Legend

X =

Date1 =

Date2 =

State =

Dear _____:

This letter responds to a letter dated March 9, 2007, submitted by X's authorized representative on behalf of X, requesting relief under § 1362(f) of the Internal Revenue Code.

FACTS

The information submitted states that X was incorporated on Date1 under the laws of State and on or about that time elected to be an S corporation. On Date2, X engaged in an event that terminated X's S corporation election. In connection with this event, on Date2 X also may have created a second class of stock, and this would have terminated X's S corporation election had the election not already terminated on Date2.

X represents that it did not intend to terminate its S corporation election and that it has consistently filed its tax returns consistent with its treatment as an S corporation. As soon as X discovered the terminating event, X initiated corrective action in order to

once again become a small business corporation. In addition, X eliminated the possible second class of stock. X and its shareholders have agreed to make such adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary.

LAW AND ANALYSIS

Section 1361(a)(1) provides that the term “S corporation” means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) defines the term “small business corporation” as a domestic corporation which is not an ineligible corporation and that does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than one class of stock.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the first day of the first taxable year for which the corporation is an S corporation) the corporation ceases to be a small business corporation.

Section 1362(f) provides that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2) or (3); (2) the Secretary determines that the circumstances resulting in termination was inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in the termination, steps were taken so that the corporation is a small business corporation; and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in the termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4(b) of the Income Tax Regulations provides that the determination of whether a termination was inadvertent is made by the Commissioner. The corporation has the burden of establishing that under the relevant facts and circumstances the Commissioner should determine that the termination was inadvertent. The fact that the terminating event was not reasonably within the control of the corporation and was not part of a plan to terminate the election, or the fact that the event took place without the knowledge of the corporation, notwithstanding its due diligence to safeguard itself against such event, tends to establish that the termination was inadvertent.

CONCLUSION

Based solely on the facts submitted and representations made, we conclude that X's S corporation election was terminated on Date2 and that this termination was inadvertent within the meaning of § 1362(f).

Under § 1362(f), X will be treated as if it were an S corporation from Date2 and thereafter, provided that X's S corporation election on Date1 was valid and was not terminated under § 1362(d) for reasons other than the events described above on Date2. Accordingly, all of the shareholders of X, in determining their respective income tax liabilities for the period beginning Date2 and thereafter, must include their pro rata share of the separately and nonseparately computed items of X as provided in § 1366, make any adjustments to basis as provided in § 1367, and take into account any distributions made by X as provided in § 1368. If X or its shareholders fail to treat themselves as described above, this ruling shall be null and void.

Except as expressly set forth above, we express or imply no opinion concerning the federal income tax consequences of the facts described above under any other provision of the Code. Specifically, we express or imply no opinion concerning whether X was eligible to make the S corporation election or whether X otherwise qualifies as an S corporation.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

James A. Quinn
Senior Counsel, Branch 3
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2):

Copy of this letter

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